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SUBJECT: NEW CONFLICT OF INTEREST LAW: IMPROVED, BUT NOT ENOUGH

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¶1. (SBU) SUMMARY: Montenegro's new Law on the Conflict of Interest, adopted in January, restricts the private business activities of public officials. But while many observers concede that it is a step forward from the roundly criticized previous law, they question the independence of the commission charged with reviewing conflict of interest cases and express concerns over the absence of more severe penalties. The law also appears to have some major blind spots, as in the recent case of a GoM loan to a bank partially owned by the PM's brother (and the PM himself, via a blind trust) attests. END SUMMARY.

Montenegro Adopts New Conflict of Interest Law

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¶2. (SBU) The adoption of a new Conflict of Interest Law has been on the GoM's plate for some time. The European Commission and the Group of States Against Corruption (GRECO) had sharply criticized the previous 2004 law - which Vanja Calovic of the anti-corruption NGO MANS publicly called "the worst in the region," because of a number of loopholes. As a result the GoM was under considerable pressure to pass a better bill.

¶3. (U) After a lengthy saga, on January 9, President Vujanovic finally signed the new law, which among other things:

--defines public officials, whether appointed or elected, who are covered;

--requires officials to declare all income and transfer management of companies they own to another person within 15 days of taking a government job;

--forbids public officials from directing or serving on the boards of businesses and non-state public corporations;

--restricts post Government employment business activities (e.g., there is a one-year "pause" before a former official can do any business with the GoM);

--obliges public officials to refer to the Commission any question about a potential conflict of interest

(i.e., before engaging in business activity, etc.);

--bans gifts over 50 Euros; and

--establishes a system of sanctions (fines, and in more serious cases, referrals to the prosecutor) for infringements.

¶4. (SBU) As was the case with the previous law, the new law establishes a seven-person Commission to review income statements and possible conflicts of interest. But unlike the previous law, under the new law, members of the Commission may not belong to a political party.

Still Plenty of Flaws

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¶5. (SBU) While generally praising the new law, both international and domestic observers have noted a number of flaws in the legislation. For example, a December 5 GRECO compliance report criticized the fact that the law does not cover all public officials. Likewise, an EC assessment noted that:

--although Commission members may not belong to political parties, their independence could be compromised by the fact that they are confirmed by Parliament and are nominated by the Parliament's Administrative Board;

--it is unclear how the Commission receives allegations of violations, and whether a judicial review by an administrative court is possible;

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--there is no recusal system; and

--the penalties (fines) envisioned by the law are limited, and the Commission is not permitted to remove officials from office.

¶6. (SBU) During the parliamentary debate over the law, opposition parties also proposed more than two dozen amendments which they said would toughen the law. In addition to the issues outlined above, opposition MPs charged that the new law allows MPs to sit on the boards of state-owned companies -- though the law forbids GoM officials from doing so. The opposition also argued for more stringent sanctions.

President's Veto... Weakens Law

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¶7. (SBU) After Parliament passed the new law on December 15 (the opposition abstained), President Vujanovic vetoed it, citing an inconsistency - namely, that public officials serving on the boards of state-majority owned companies could receive compensation, while public officials serving on the boards of scientific, humanitarian, and sports associations could not. (Note: Vujanovic had vetoed a previous draft as well, at that time asserting that public officials should not be permitted to serve on the boards of any state-owned company. End Note.)

¶8. (SBU) In late December, Parliament responded by allowing compensation for all officials, including those on the boards of non-commercial associations (rather than forbidding it for officials serving on boards of state companies). In addition, Predrag Boskovic, an MP of the ruling Democratic Party of Socialists (DPS) who is on the board of the coal mine in northern Montenegro, inserted a clause from the old law which allowed MPs to serve on the boards of any company with a state stake, no matter how small (the earlier version of the new law specified that the state had to have a majority stake). According to Calovic, President Vujanovic did not veto the bill a third time, because the rest of the GoM leadership wanted the law passed.

Blind To The Biggest Conflicts?

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¶9. (SBU) The law also appears to concern only public officials and members of their "household" (i.e. immediate family) - but not other relatives - and does not limit officials who place property or assets in a blind trust. These loopholes were brought into stark relief in the controversy surrounding Prva Banka, Montenegro's largest domestic bank, which has recently encountered severe financial difficulties.

¶10. (SBU) Prva Banka has strong links to family and friends of PM Milo Djukanovic. The PM's brother, Aco Djukanovic, who bought into the bank in 2007, is its largest shareholder. The PM's sister, Ana Kolarevic, has a small stake, and the managing board of the bank includes a number of Djukanovic cronies. In August 2007, Milo Djukanovic himself, who was then out of government, took a 1.5 million Euro loan from an obscure London bank to purchase shares in Prva Banka through his company Capital Invest.

¶11. (SBU) Critics contend that DPS officials encouraged state-owned companies (and private companies as well) to shift deposits to Prva Banka. The bank expanded rapidly, with assets growing from 29 million Euros in June 2006 to 546 million Euros in mid-2006. But the bank's allegedly lax lending practices - often to DPS cronies, according to critics - landed it in financial hot water when the global economic crisis began. And as the bank foundered, the following sequence of events occurred:

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--In late October, Parliament passed a new Law on Measures to Protect the Banking System (reftel), which permitted the GoM to grant loans to banks in return for shares as collateral; in addition, the amount of the loan could not be more than the nominal value of the shares.

--On November 25, Prva Banka's two biggest shareholders, Aco Djukanovic and Montenegro's (state-owned) electricity company (Elektroprivreda Crne Gore - EPCG) participated in a re-capitalization of the bank worth 20 million Euros; Aco's share of the bank increased to 46.48 percent, and EPCG's share went from 9.46 percent to 18.24 percent. Milo Djukanovic's Capital Invest ended up with 2.86 percent; and with his sister's one percent share, the Djukanovic family is now the majority shareholder. The opposition also noted that EPCG put six

million Euros (as "an investment") into the recapitalization at a time when that company was experiencing its own financial difficulties (EPCG had just decided to raise electricity prices to consumers). Overall, Prva Banka's nominal value increased from 26.7 million to 46.7 million Euros.

--On November 28, immediately following the recapitalization, Prva Banka requested a 40 million Euro loan (an amount made possible by the bank's recapitalization) to improve its liquidity. Despite protests from the opposition - who pointed out that the government was supporting a bank controlled by the PM's family and friends - the GoM (from the budget and administered through the Ministry of Finance) granted a three-month loan at a 2.5 percent interest rate; however, the terms of the loan allowed the repayment period to be extended to one year. The PM told Parliament in December that the GoM had stepped in to protect Prva Banka's depositors, not its shareholders.

¶12. (SBU) At least one opposition party appealed to the Commission on Conflict of Interest to ascertain the legality of granting a loan to a bank in which the PM's brother is the largest shareholder. MANS' Calovic told us that she had consulted with several lawyers on the question, who agreed that the PM did not violate either the old or new laws on conflict of interest. According to Calovic, since Aco Djukanovic is not a member of the PM's "household," his ownership of Prva Banka shares does not constitute a conflict of interest. Moreover, as long as the PM had put his own shares into a blind trust - he was required to hand over the management of his company Capital Invest to another person when he returned to head the GoM in 2008 - the PM was also in the clear, according to the letter of the law.

Comment

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¶13. (SBU) A number of our interlocutors, including opposition political leaders and Calovic, have told us that the new law on conflict of interest is an improvement over the old one. However, as the Prva Banka case demonstrates, it contains some massive loopholes. In addition, implementation of the law has been lackluster. The Commission on Conflict of Interest referred only five cases to the prosecutor between 2004 and 2008, and the press recently reported that less than 20 percent of public officials filed the required income declarations last year. The authorities clearly need to do a better job of enforcing the provisions that the law does stipulate.

KONTOS